REPORT ON EXAMINATION

OF THE

EVEREST REINSURANCE COMPANY

AS OF

DECEMBER 31, 2006

I, Matthew Denn, Insurance Commissioner of the State of Delaware, do hereby certify that the attached REPORT ON EXAMINATION, made as of DECEMBER 31, 2006 of the

EVEREST REINSURANCE COMPANY

is a true and correct copy of the document filed with this Department.

Antoinette Handy

ATTEST BY:

DATE: 27TH JUNE 2008



In Witness Whereof, I have hereunto set my hand and affixed the official seal of this Department at the City of Dover, this 27TH day of JUNE 2008.

Insurance Commissioner

REPORT ON EXAMINATION

OF THE

EVEREST REINSURANCE COMPANY

AS OF

December 31, 2006

The above captioned Report was completed by examiners of the Delaware Insurance Department.

Consideration has duly been given to the comments, conclusions, and recommendations of the examiners regarding the status of the Company as reflected in the Report.

This Report is hereby accepted, adopted, and filed as an official record of this Department.

MATTHEW DENN INSURANCE COMMISSIONER

DATED this 27TH Day of JUNE 2008.

TABLE OF CONTENTS	Page
SALUTATION	1
SCOPE OF EXAMINATION	2
HISTORY	3
CAPITALIZATION	4
DIVIDENDS TO STOCKHOLDER	5
MANAGEMENT AND CONTROL	6
INSURANCE HOLDING COMPANY SYSTEM	8
AGREEMENTS	10
TERRITORY AND PLAN OF OPERATION	13
REINSURANCE	17
Assumed Ceded	18 20
GROWTH OF THE COMPANY	22
ACCOUNTS AND RECORDS	23
FINANCIAL STATEMENTS	24
ANALYSIS OF ASSETS LIABILITIES, SURPLUS AND OTHER FUNDS UNDERWRITING AND INVESTMENT EXHIBIT - STATEMENT OF INCOME CAPITAL AND SURPLUS ACCOUNT	24 25 26 27
NOTES TO FINANCIAL STATEMENTS	27
COMPLIANCE WITH PRIOR RECOMMENDATIONS	30
RECOMMENDATIONS	31
CONCLUSION	32
SUBSEQUENT EVENTS	33

SALUTATION

Honorable Alfred W. Gross Chairman – Financial Condition (E) Committee, NAIC State Corporation Committee Bureau of Insurance P.O. Box 1157 Richmond, VA 23218

Honorable Julie Mix McPeak Secretary, Southeastern Zone (II), NAIC Office of Insurance Commonwealth of Kentucky P.O. Box 517 Frankfort, KY 40602-0517

Honorable Morris Chavez Secretary, Western Zone (IV), NAIC Superintendent, New Mexico Public Regulation Commission, Insurance Division 1120 Paseo de Peralta Santa Fe, NM 87504-1269 Honorable Steven M. Goldman Secretary, Northeastern Zone (I), NAIC Commissioner of Insurance State of New Jersey Department of Insurance and Banking 20 West State Street, 11th Floor P.O. Box 325 Trenton, NJ 08625-0325

Honorable Merle D. Scheiber Secretary, Midwestern Zone (III), NAIC South Dakota Division of Insurance Department of Revenue and Regulation 445 East Capitol Avenue Pierre, SD 57501-3185

Honorable Matthew P. Denn Insurance Commissioner State of Delaware Department of Insurance 841 Silver Lake Boulevard, Suite 100 Dover, DE 19904

Commissioners:

In compliance with your instructions and pursuant to statutory provisions contained in Certificate of Authority letter 07.007 dated September 18, 2007, an examination has been made of the affairs, financial condition and management of the

EVEREST REINSURANCE COMPANY

hereinafter referred to as "Company" or "Everest Re", incorporated under the laws of the State of Delaware. The examination was conducted at the administrative office of the Company located at 477 Martinsville Road, Liberty Corner, and New Jersey. This examination was conducted concurrently with that of affiliates Everest National Insurance Company (ENIC), Everest Indemnity Insurance Company (EIIC) and Mt. McKinley Insurance Company (McKinley), all of

which are Delaware domestic insurance companies. Separate reports of examination were filed for each company. The report of examination is respectfully submitted.

SCOPE OF EXAMINATION

The last filed examination of the Company was conducted by the Delaware Department of Insurance as of December 31, 2003. This examination covered the period January 1, 2004 through December 31, 2006, and consisted of a general survey of the Company's business practices and policies; management, any corporate matters incident thereto; a verification and evaluation of assets and a determination of liabilities. Transactions and events occurring subsequent to the latter date were reviewed and have been commented upon throughout the examination report to the extent deemed necessary.

This report is presented on an exception basis. It is designed to set forth the facts with regard to any material adverse findings disclosed during the examination. The text will explain changes wherever made. If necessary, comments and recommendations have been made in those areas in need of correction or improvement. In such cases, these matters were thoroughly discussed with responsible personnel and/or officials during the course of the examination.

The examination followed rules established by the National Association of Insurance Commissioners (NAIC) Committee on Financial Condition Examiners Handbook, as adopted by the Delaware Insurance Department under 18 <u>Del. C.</u> §526(a), and generally accepted statutory insurance examination standards.

In addition to noted items in this report, the following topics were reviewed without exception and are included in the workpapers of this examination.

Corporate Records
Fidelity Bond and Other Corporate Insurance
All Assets and Liability items not mentioned

The examination was conducted by the Delaware Department of Insurance in accordance with the Association Plan of Examination Guidelines established by the NAIC. No states participated in the examination.

Workpapers prepared by the Company's external accounting firm,

PricewaterhouseCoopers LLP, (PwC) New York, New York, in connection with the annual audit, were reviewed and relied upon to the extent possible.

INS Services, Inc. was retained by the Delaware Insurance Department to conduct a review of the Company's overall control risk related to information system controls.

HISTORY

The Company was originally incorporated as Prudential Reinsurance Company (Prudential Re) on June 13, 1973, under the laws of the State of Delaware and began operations on June 25, 1973. At that time, the Company was a wholly owned subsidiary of PRUCO, Inc. (PRUCO), which was a wholly owned holding company subsidiary of The Prudential Insurance Company of America (The Prudential).

In November 1993, Prudential Reinsurance Holdings, Inc. (Holdings) was formed for the purpose of owning all of the capital stock of Prudential Re. On December 31, 1993, PRUCO transferred all of the issued and outstanding shares of Prudential Re to Holdings in exchange for all of the issued and outstanding shares of Holdings.

On October 5, 1995, the Company entered into a Separation Agreement with The Prudential, PRUCO, and Gibraltar Casualty Company (Gibraltar). The Agreement outlined the terms and conditions of the separation of corporate relationships in such areas as record keeping, employee access, employee benefits, investment services, corporate name, directors, and service agreements.

Effective October 6, 1995, PRUCO completed an initial public offering of 100% of the outstanding common stock of Holdings and, as a result of this transaction, Prudential Re and Holdings ceased to be members of The Prudential insurance holding company system. At that time, the Company became a member of a holding company system in which Holdings was the ultimate controlling person. Thereafter, the Company, Holdings and all of Holdings' subsidiaries changed their names to replace "Prudential" with "Everest". On April 2, 1996, the Company changed its name to its present name of Everest Reinsurance Company.

Effective February 24, 2000, Holdings became a wholly owned subsidiary of Everest Re Group, Ltd. (Group), a Bermuda company, pursuant to a plan of restructuring.

CAPITALIZATION

At December 31, 2006, the Company had 25,000 common shares authorized with a par value of \$400 per share, of which all shares were issued and outstanding. The following schedule shows the changes in the Company's capital and surplus from the previous examination to the current examination.

	Common Capital Stock	Gross Paid in & Contributed <u>Surplus</u>	Unassigned Funds (<u>Surplus)</u>	<u>Total</u>
12/31/03	\$10,000,000	\$566,544,924	\$1,138,972,957	\$1,715,517,881
Operations (1)				
2004 Operations			299,476,085	299,476,085
2005 Operations			129,535,373	129,535,373
2006 Operations			468,156,637	468,156,637
Surplus Contributions (2)				
2004 Surplus Contribution		148,158,129		148,158,129
2005 Surplus Contribution		179,906,697		179,906,697
2006 Surplus Contribution		8,370,070		8,370,070
Dividend to Stockholder				
2004 Dividend Paid			(70,000,000)	(70,000,000)
2005 Dividend Paid			(75,000,000)	(75,000,000)
2006 Dividend Paid			(100,000,000)	(100,000,000)
12/31/06	\$10,000,000	\$902,979,820	\$1,791,141,052	\$2,704,120,872

- (1) Operations are defined as: Net income, change in net unrealized capital gains or (losses), change in net unrealized foreign exchange capital gain (loss), change in net deferred income tax, change in nonadmitted assets, change in provision for reinsurance and aggregate write-ins for gains and losses in surplus.
- Of the \$148,158,129 surplus contributions received in 2004, \$140,000,000 was received directly from Parent and \$8,158,129 was received indirectly from Parent related to the tax benefit of stock options exercised. Of the \$179,906,697 surplus contributions received in 2005, \$175,000,000 was received directly from Parent and \$4,906,697 was received indirectly from Parent related to the tax benefit of stock options exercised. Of the \$8,370,070 surplus contributions received in 2006, there was no direct contribution received from Parent and \$8,370,070 was received indirectly from Parent related to the tax benefit of stock options exercised.

DIVIDENDS TO STOCKHOLDER

The Company is subject to statutory and regulatory restrictions imposed by the State of Delaware on insurance companies, which limit the amount of cash dividends that may be paid to the shareholder. Under Delaware law, cash dividends may be paid only from realized net profits and realized capital gains. Additionally, the maximum aggregate amount of ordinary dividends that the Company may declare or pay during any twelve-month period is the greater of (1) 10% of its statutory surplus or (2) net income, not including realized capital gains, each as reported in

the prior year's annual statements, unless written approval by the Delaware Insurance Commissioner granting a greater amount is obtained (extraordinary dividends). In addition, no dividend may be paid in excess of unassigned surplus.

According to Company records and as reflected in minutes to the Board of Directors' meetings, cash dividends to Stockholder of \$245,000,000, as reflected below, represent ordinary dividends, declared and paid by the insurer in accordance with 18 Del. C. §5005(b):

February 23, 2004 March 11, 2004 \$15,000	,000
	•
September 8, 2004 September 20, 2004 30,000	
December 8, 2004 December 20, 2004 25,000	,000
March 15, 2005 March 25, 2005 25,000	,000
June 15, 2005 June 29, 2005 25,000	,000
September 15, 2005 September 28, 2005 25,000	,000
March 15, 2006 March 29, 2006 25,000	,000
June 15, 2006 June 29, 2006 25,000	,000
September 7, 2006 September 28, 2006 25,000	,000
December 6, 2006 December 28, 2006 25,000	,000
Total \$245,000	,000

MANAGEMENT AND CONTROL

Pursuant to the General Corporation Law of the State of Delaware, as implemented by the Company's Certificate of Incorporation and bylaws, all corporate powers and its business property and affairs are managed by, or under the direction of, its Board of Directors (Board). The Board shall consist of at least seven members and is not subject to a maximum.

The Board of Directors at December 31, 2006, was comprised of seven members. With the exception of Mr. Eisenacher, who was elected by written consent of the sole shareholder effective December 18, 2006, upon the resignation of Stephen Limauro, all of the directors were elected by written consent of the sole shareholder effective June 21, 2006. Each director shall hold office until his successor is elected and qualified, or until earlier resignation or removal.

The members of the Board of Directors serving as of December 31, 2006, were as follows:

<u>Director's Name</u>	Principal Business Affiliation
Joseph Victor Taranto, (Chairman)	Everest Reinsurance Company
Scott Philip Callahan	Everest Reinsurance Company
Craig Edward Eisenacher	Everest Reinsurance Company
Larry Allen Frakes	Everest Reinsurance Company
Thomas James Gallagher	Everest Reinsurance Company
Steven A Mestman	Everest Reinsurance Company
David Edward Schmitt	Everest Reinsurance Company

The Company's bylaws provide for the Board, by resolution or resolutions passed by a majority of the Board, to designate one or more committees, each committee to consist of three or more directors of the corporation. The Board may also designate one or more directors as alternate members of any committee, who may replace any absent or disqualified member at any meeting of the committee.

The Company had the following three active committees as of December 31, 2006: Salary and Compensation Committee, Executive Committee and Investment Committee.

The Board members serving on each of the committees were as follows:

Joseph Victor Taranto Thomas James Gallagher Craig Edward Eisenacher

The bylaws of the Company state that the principal officers include a Chairman of the Board, a Chief Executive Officer, a President, a Treasurer, a Comptroller, a Secretary (of whom only the Chairman of the Board and Chief Executive Officer need be a director of the corporation), and one or more Vice Presidents, Assistant Treasurers, Assistant Comptroller, Assistant Secretaries, and such other officers, assistant officers or agents (none of whom need be a director) as the Board of Directors from time to time may determine.

At December 31, 2006, the Company's principal officers and their respective titles were as follows:

<u>Officer</u>	<u>Title</u>
Joseph Victor Taranto	Chairman and Chief Executive Officer
Thomas James Gallagher	President and Chief Operating Officer
Craig Edward Eisenacher	Executive Vice President and Chief Financial Officer
Sanjoy Mukherjee	Senior Vice President, General Counsel, Secretary and
	Compliance Officer
Scott Phillip Callahan	Executive Vice President, U.S. Property
Steven A Mestman	Executive Vice President, Treaty Casualty
Larry Allen Frakes	Executive Vice President, Direct Operations
David Edward Schmitt	Executive Vice President, International
Barry Howland Smith	Executive Vice President and Chief Administrative Officer
Gary Irwin Koupf	Senior Vice President and Actuary
Frank Nicholas Lopapa	Senior Vice President and Treasurer
Daryl Wayne Bradley	Senior Vice President

The minutes of the meetings of the Stockholder and Board of Directors, which were held during the period of examination, were read and noted. Attendance at meetings, election of directors and officers and approval of investment transactions were also noted.

Inspection of Company files indicated that ethics statement/conflict of interest affidavits were distributed, completed and returned by all employees at a manager level or above for the examination period. During our review for compliance with 18 <u>Del. C.</u> §4919, it was noted that the Company properly reported changes in directors and principal officers.

INSURANCE HOLDING COMPANY SYSTEM

The Company is a member of an insurance holding company system as defined in 18 <u>Del.</u>

<u>C.</u> §5001(4) "Insurance holding company system". The Company's Holding Company registration statements were properly filed by the Company with the Delaware Insurance Department.

All of the common stock is owned by Holdings, a Delaware domiciled holding company. The ultimate controlling entity of the holding company system is Group. Group's stock is traded on the New York Stock Exchange under the symbol "RE". As of December 31, 2006, Group, on a consolidated U.S. Generally Accepted Accounting Principles basis (GAAP), reported approximately \$17.1 billion in assets and \$5.1 billion in shareholders equity.

The Company has four wholly owned subsidiaries at December 31, 2006, with domicile shown in parentheses: Everest National Insurance Company (Delaware); Everest Indemnity Insurance Company (Delaware); Everest Insurance Company of Canada (Canada); and Everest Security Insurance Company (Georgia).

The Company sold its United Kingdom branch on January 1, 2004, to affiliate Everest Re Reinsurance (Bermuda), Ltd. (ERBL), a subsidiary of the Company's ultimate parent, Everest Re Group, Ltd. The sales agreement included a fixed sale price of \$77 million in exchange for the net assets of the branch. The Company realized a net capital loss of \$3.95 million on the sale. In connection with the sale, the Company provided a reserve indemnity agreement providing for indemnity payments of up to 90% of \$44.51 million of the excess of 2002 and prior loss and loss adjustment expense (LAE) reserves, provided that any recognition of profit from the reserves for 2002 and prior underwriting years are taken into account. The Company is fully reserved under this reserve indemnity agreement at December 31, 2006 (See the Subsequent Events section of this report for additional information).

The Company voluntarily dissolved its Bermuda subsidiary, Everest Re Holdings, Ltd., on January 27, 2006. As a result of the dissolution, the net assets and surplus of the subsidiary were distributed to the Company. The amount of the distribution was approximately \$78 million.

The following organizational structure, of which the Company is a part, illustrates the identities and relationships between its parent, affiliates and subsidiaries as of December 31, 2006.

	Domicile	% Ownership
Everest Re Group, Ltd.	Bermuda	70 Ownership
Everest Re Advisors, Ltd.	Bermuda	100%
Everest Advisors (Ireland) Limited	Ireland	100%
Everest Advisors (UK), Ltd.	United Kingdom	
Everest Reinsurance (Bermuda), Ltd.	Bermuda	100%
Everest Global Services, Inc.	Delaware	100%
Everest International Holdings, Ltd.	Bermuda	100%
Everest International Reinsurance, Ltd.	Bermuda	100%
Everest Reinsurance Holdings, Inc.	Delaware	100%
Everest Re Capital Trust	Delaware	100%
Everest Re Capital Trust II	Delaware	100%
Mt. McKinley Insurance Company	Delaware	100%
Mt. McKinley Managers, LLC		100%
Workcare Southeast, Inc.	New Jersey Alabama	100%
Workcare Southeast of Georgia, Inc.	Georgia	100%
Everest Reinsurance Company	Delaware	100%
Everest National Insurance Company	Delaware	100%
Everest Insurance Company of Canada	Canada	100%
Everest Indemnity Insurance Company	Delaware	100%
Everest Security Insurance Company	Georgia	100%

AGREEMENTS

Service Agreements

The Company has service agreements with its affiliates. Under these agreements, the Company and its affiliates provide each other the service of its employees, supplies, use of equipment and office space and makes payment to third parties for general expenses and state and local taxes. The agreements obligate the affiliate to reimburse the company providing the services for disbursements made on their behalf and to pay for the cost of providing those services.

These agreements were replaced with a new service agreement effective January 1, 2008, as detailed in the "Subsequent Events" section of this report.

Tax Allocation Agreement

Effective January 1, 2001, the Company entered into a tax allocation agreement with Holdings along with its affiliates. Holdings, the Company and affiliates constitute an affiliated group within section 1504(a) of the Internal Revenue Code of 1986 of which Holdings is the common parent and, therefore, is eligible to file a consolidated income tax return for United States federal income tax purposes and to pay federal income taxes on a consolidated basis, if necessary. Pursuant to the terms of the tax allocation agreement, no party will be required to pay more in taxes, or receive a lesser refund, than it would have paid or received if it computed its taxes independently and filed a separate tax return.

Guarantee Agreements

Effective September 30, 2002, the Company entered into a parental guarantee agreement with EIIC. The agreement, as approved by the Delaware Department of Insurance, states that the Company guarantees EIIC's obligations up to \$50 million. There was no activity related to this agreement during the period under examination.

Effective April 26, 2003, the Company entered into a parental guarantee agreement with ENIC. Since the agreement does not expose the assets of the Company to any liabilities, it was not subject to Arizona's filing requirements (ENIC was domiciled in Arizona until its redomestication to Delaware effective November 30, 2005). According to the Agreement, Everest Re guarantees that ENIC's capital and surplus will not fall below \$15 million. Furthermore, this agreement is subject to an aggregate of \$75 million. There was no activity related to this agreement during the period under examination.

<u>Investment Advisory Agreement – Domestic Operations</u>

The Company and its affiliates share a common investment manager for domestic operations, Deutsche Investment Management Americas, Inc. (Deutsche). The agreement, effective July 1, 1996, authorizes Deutsche to supervise and direct all domestic investments and to exercise whatever powers the Company may possess with respect to its domestic invested assets. Investment transactions will be in accordance with investment objectives of the Company and subject to restrictions established by the Company, as communicated to Deutsche in writing from time to time. Deutsche is the investment manager for the Everest Re Group and fees are reflective of total assets under management.

<u>Investment Advisory Agreement - International Operations</u>

The Company has an investment manager for its international operations, Deutsche Asset Management International GmbH (Deutsche International), effective September 30, 2005. This agreement authorizes Deutsche International to supervise and direct all international investments and to exercise whatever powers the Company may possess with respect to its international invested assets. Investment transactions will be in accordance with investment objectives of the Company and subject to restrictions established by the Company, as communicated to Deutsche International in writing from time to time. This agreement replaced an earlier similar agreement dated April 5, 2002. The total investment expenses incurred by the Company for 2006 with Deutsche and Deutsche International advisors were approximately \$2.1 million.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2006, the Company was licensed as a property and casualty insurer and/or reinsurer in all states (except Nevada, New Hampshire and Wyoming), the District of Columbia, Canada, and is authorized to conduct reinsurance business in Singapore and the United Kingdom (license surrendered in 2004 with the sale of the U.K. branch detailed earlier). Everest Re can also write reinsurance in other foreign countries. As some jurisdictions require a reinsurer to register, Everest Re is registered as a foreign insurer and/or reinsurer in the following countries: Argentina, Bolivia, Chile, Colombia, Ecuador, Guatemala, Mexico, Peru, Venezuela, and the Philippines.

The Company underwrites property and casualty reinsurance on a treaty and facultative basis for insurance and reinsurance companies in the United States and selected international markets. The Company underwrites reinsurance through both brokers and directly with insurance companies, giving it the flexibility to pursue business regardless of the ceding company's preferred reinsurance purchasing method. The majority of the Company's business is written in the United States on domestic risks. International business was written out of the home office and branch operations in Miami, Belgium, Canada, Hong Kong and Singapore.

The Company and its insurance subsidiaries (excluding Mt. McKinley) had a rating of "A+" (Superior) by A.M. Best.

Net written premium for 2006 was \$2.187 billion, a decrease of \$778 million from the \$2.965 billion reported in 2003. The decrease can be attributed to various lines of business, with group accident and health, workers compensation, private passenger auto liability, auto physical damage and non-proportional assumed liability reinsurance business accounting for the largest decreases. Ceded premiums decreased to \$900 million in 2006 from \$1.215 billion in 2003. Of

the total ceded premiums, \$775 million, or 86.2%, were ceded to affiliates during 2006 under the global quota share treaties with affiliates ERBL and Everest International Reinsurance, Ltd. (EIRL).

As of December 31, 2006, the Company reported in the annual statement the following distribution of net premiums:

Fire	\$143,904,035
Allied lines	54,751,789
Farmowners multiple peril	1,957,230
Homeowners multiple peril	199,691,514
Commercial multiple peril	170,513,312
Mortgage guaranty	175,429
Ocean marine	37,978,482
Inland marine	9,670,603
Financial guaranty	314,697
Medical malpractice – occurrence	291,525
Medical malpractice – claims made	710,523
Earthquake	46,149,995
Group accident and health	59,732,203
Credit and other accident and health	3,159,688
Workers' compensation	186,815,471
Other liability – occurrence	271,978,593
Other liability – claims made	203,058,043
Products liability- occurrence	4,187,682
Private passenger auto liability	16,362,916
Commercial auto liability	28,581,295
Auto physical damage	13,224,724
Aircraft	21,071,192
Fidelity	2,375,421
Surety	66,406,468
Burglary and theft	3,646,361
Boiler and machinery	19,627,917
Credit	16,301,066
International	2,109
Reinsurance (a)	398,130,237
Reinsurance (b)	202,276,795
Reinsurance (c)	4,080,681
Total	\$2,187,127,996

- (a) Non proportional assumed property
- (b) Non proportional assumed liability
- (c) Non proportional assumed financial lines

Group operations are divided into four underwriting segments: U.S. Reinsurance Operations, U.S Insurance Operations, Specialty Underwriting Operations, and International Operations.

U.S. Reinsurance Operations

U.S. Reinsurance Operation writes property and casualty reinsurance, both treaty and facultative, through reinsurance brokers as well as directly with ceding companies within the United States. The Company targets certain brokers and, through the broker market, specialty companies and small to medium sized standard lines companies. On a direct basis, the Company targets companies which place their business predominantly in the direct market, including small to medium sized regional ceding companies. In addition, the U.S. Reinsurance Operation writes portions of reinsurance programs for larger, national insurance companies. The treaty casualty portfolio consists principally of professional liability, D&O liability, workers' compensation, excess and surplus lines, and other liability coverages. The facultative unit conducts business both through brokers and directly with ceding companies and consists of three underwriting units representing property, casualty and specialty lines of business. Business is written from a facultative headquarters office in New York with satellite offices in Chicago and San Francisco. The U.S. Reinsurance Operation gross written premium for 2006 was distributed as follows:

U.S. treaty casualty business accounted for \$492 million of gross business in 2006; U.S. treaty property business accounted for \$587 million in gross business.

The Company's facultative unit in 2006 wrote \$71 million in property business, \$107 million in casualty, \$13 million in specialty business and \$25 million in national brokerage business.

U.S. Insurance Operations

The U.S. Insurance Operation writes property and casualty insurance primarily through general agent relationships and surplus lines brokers within the United States. Most of the business was written by ENIC and EIIC, which primarily writes commercial property and casualty business through program administrators. The Company wrote approximately \$13 million of premium on a pro rata basis, \$10 million in casualty and \$3 million in property in 2006.

Specialty Underwriting Operations

The Specialty Underwriting Operation writes accident and health (A&H), marine, aviation and surety business within the United States and worldwide through brokers and directly with ceding companies. The A&H unit primarily focuses on health reinsurance of traditional indemnity plans, self-insured health plans and specialty medical plans. The marine and aviation unit focuses on ceding companies with a particular expertise in marine and aviation business. The marine and aviation business is written primarily through brokers and contains a significant international component written primarily in the London market. Surety business underwritten by the Company consisted mainly of reinsurance of contract surety bonds. Specialty Underwriting Operations produced \$251 million of gross written premium for 2006 which was distributed as follows:

In 2006, the marine and aviation unit produced approximately \$97 million of premium, substantially all of which was written on a treaty basis through reinsurance brokers.

In 2006, the surety unit wrote about \$71 million of premium of which almost all was written on a pro rata basis.

In 2006, the A& H unit totaled \$83 million of premium mostly written through brokers.

International Operations

The Company's International Operations are designed to enable it to capitalize on the growth opportunities in the international reinsurance market. The Company targets several international markets including: Europe; Canada, with a branch in Toronto; Asia, with a branch in Singapore; Latin America, Africa and the Middle East, which business is serviced from Everest Re's New Jersey headquarters and its Miami office. The Company also writes "homeforeign" business, which provides reinsurance on the international portfolios of U.S. Insurers, from New Jersey. The Company wrote approximately \$436 million in home-foreign business. The Brussels office focuses on the continental European reinsurance markets and is ceded to Bermuda. The Company's Singapore branch covers the Asian markets and wrote approximately \$143 million in gross written premium. The Canadian branch wrote approximately \$172 million in gross written premium.

REINSURANCE

The Company assumes all authorized lines of business from affiliates and non-affiliates on both a treaty and facultative basis. During the examination period, the Company decreased its assumptions from affiliates. In 2006, inter-company assumptions amounted to \$774 million, of which \$497 million was assumed from ENIC, \$254 million from EIIC and \$23 million from ESIC.

For 2006, the Company reported the following distribution of net premiums written:

Direct Written Premiums	\$ 13,473,490
Reinsurance assumed (from affiliates)	774,611,667
Reinsurance assumed (from non-affiliates)	2,298,758,892
Total Assumed Premiums	3,073,370,559
Gross Written Premiums	3,086,844,049
Reinsurance ceded (to affiliates)	775,340,711
Reinsurance ceded (to non-affiliates)	124,375,342
Total Ceded Premiums	899,716,053
Net Written Premiums	\$ <u>2,187,127,996</u>
Percentage of Ceded to Gross	29.1%

<u>Assumed</u>

Non-Affiliates

The Company assumes both property and casualty reinsurance on a treaty and facultative basis through reinsurance brokers and on a direct basis. All reinsured clients are evaluated for financial stability and performance results. Reinsurance is assumed on both a pro rata and excess of loss basis. The Company assumes business from approximately 500 entities at December 31, 2006.

The following table details the breakdown of assumed business by branch:

Operating Segment	<u>Total</u>
U.S. Reinsurance	\$2,757,048,666
International	
Belgium	983,784
Canada	172,298,685
Hong Kong	(23,191)
Singapore	143,062,615
Total	\$ <u>3,073,370,559</u>

The following entities represent at least 2% of 2006 non-affiliated assumed premiums:

Entity	Domicile	Assumed Premiums
American Home Assurance Company	New York	\$161,468,000
Continental Casualty Company	Illinois	57,006,000
Factory Mutual Insurance Company	Rhode Island	47,038,000
Great American Insurance Company	Ohio	64,029,000
Liberty Mutual Fire Insurance Company	Massachusetts	214,187,000
Universal Property and Casualty Ins Co.	Florida	112,131,000
Ace American Insurance Company	Bermuda	46,873,000
Arch Reinsurance Ltd.	Bermuda	94,309,000
North Carolina Farm Bureau Mutual	North Carolina	61,233,000
Lloyds of London	Great Britain	<u>79,629,000</u>
Total		\$937,903,000

<u>Affiliates</u>

The Company assumes business from various affiliates through global and business-specific quota share and excess of loss reinsurance agreements as follows:

<u>Type</u>	Business Covered	<u>Effective</u>	2006 Assumed Premiums
Everest National			
Insurance Company			
85% quota share	Global	1/1/98	\$471,040,917
Quota share and XOL	Program-specific	various	26,725,204
Subtotal ENIC	-		\$ <u>497,766,121</u>
Everest Indemnity			
Insurance Company			
85% quota share	Global	12/10/97	\$171,945,087
Quota share and XOL	Program-specific	various	82,085,725
Subtotal EIIC	C I		\$254,030,812
			,
Everest Security			
Insurance Company			
85% quota share	Global	1/1/00	\$ 22,814,734
Total			\$774,611,667

<u>Ceded</u>

Non-Affiliates

In 2006, the Company retained approximately 70.9% of direct and assumed premiums. Management estimates that the Company's greatest catastrophe exposure worldwide from any single event is to a Southeastern U.S. windstorm, where the Company estimates it has a pre-tax probable maximum loss (PML) exposure after reinsurance of approximately \$471 million. The Company further estimates that its next largest pre-tax PML exposure relates to a European windstorm of \$462 million and an earthquake affecting the west coast of \$350 million.

All reinsurance agreements reviewed were evaluated in accordance with SSAP No. 62 of the NAIC Accounting Practices and Procedures Manual. Each of the agreements cited included the required appropriate contractual clauses.

The retrocession protection during 2006 was as follows:

(1) Accident Year Aggregate Excess - Stop Loss

The Company had purchased corporate-level retrocession reinsurance covering accident year accumulations of all exposures. For the years ended 1999, 2000 and 2001, the accident year stop loss agreements provide up to \$175 million in excess of a 71% loss ratio. The purchased protection was placed 100% with London Life and Casualty Reinsurance Corporation (Barbados domiciled) for the 1999 and 2000 accident years and 100% with London Life and General Reinsurance Company, Ltd. (Ireland domiciled) for the 2001 accident year, collectively referred to as London Life. As of December 31, 2003, the Company ceded the maximum limits under all three contracts. During 2006, the Company reduced funds held by approximately \$123 million. Total outstanding recoverable at December 31, 2006 was \$52.1 million. During 2007 the Company drew down on collateral associated with these contracts.

Subsequent to the examination date, the Company entered into arbitration with London Life Reinsurance Group related to the aggregate stop loss reinsurance contracts in effect for accident years 1999, 2000 and 2001. On March 1, 2008 the Company received notification that an arbitration panel ruled against the Company on the 2001 accident year only. The Company returned collateral drawn down and rescinded the 2001 contract. The effect of this ruling on the Company's surplus is a decrease of \$45,598,421. (See the Subsequent Events section of this report).

(2) Calendar Year Aggregate Excess - Stop Loss

The Company purchased corporate-level retrocession reinsurance covering calendar year accumulations of all exposures. The 1990 3-year treaty provides up to \$45 million for each of the calendar years (1990, 1991 and 1992) and \$100 million aggregate for the 3-year period in excess of following loss ratios: 80% for 1990; 77.5% for 1991; 76.5% for 1992. The 1992 5-year treaty provides up to \$100 million for each calendar year (1992, 1993, 1994, 1995 and 1996) and \$200 million aggregate for the 5-year period in excess of a 79% loss ratio for all five years. The purchased protection was placed 100% with Continental Insurance Company (New Hampshire domiciled) for the 1990 and 1992 treaties. As of December 31, 2003, the Company ceded the maximum \$45 million under the 1990 treaty relating entirely to the 1990 calendar year. As of December 31, 2003, the Company ceded the maximum \$100 million under the 1992 treaty relating entirely to the 1992 calendar year. During 2006, the Company incurred no additional premium related to the Continental cessions (accounted for on a funds held basis). At December 31, 2006, funds held under this treaty were \$66.9 million.

The Company has not purchased similar corporate level reinsurance coverage's since 2001.

Affiliates

The Company cedes business to affiliates through global and business-specific quota share reinsurance agreements as follows:

				2006 Ceded
<u>Type</u>	<u>Business</u>	Affiliate	Effective	<u>Premiums</u>
Quota Share (3)	Casualty	Various	1/1/02	\$ 658,356,456
50% Quota Share (1)	Canadian Property	ERBL	1/1/03	43,527,767
Loss Portfolio Transfer	Net Liabilities	ERBL	10/1/01	994,645
Excess of Loss (2)	Workers Comp.	ERBL	1/1/02	(3,074)
Subtotal				\$ 702,875,794
Quota Share (3)	Property	EIRL	1/1/02	72,464,917
Total				\$ 775,340,711

- (1) Amended to 60% effective 1/1/07
- (2) \$50,000 XS \$100,000, terminated 12/31/02
- (3) The following table reflects cession percentages

	<u>Bern</u>	<u>nuda</u>	Internat	<u>ional</u>
<u>Year</u>	Casualty	Property	Casualty	Property
2002	20%	20%		
2003	25%	25%		
2004/05	22.5%	22.5%	2.5%	2.5%
2006	31.5%	18%	3.5%	2.0%
2007	31.5%	22.5%	3.5%	2.5%

GROWTH OF THE COMPANY

The following information was obtained from the Company's filed Annual Statements and covers the period from the prior examination to December 31, 2006:

<u>Year</u>	Net Written Premiums	Net Admitted <u>Assets</u>	<u>Liabilities</u>	Common <u>Stock</u>	Gross paid in and contributed surplus	Unassigned Funds (surplus)	Net Income
2003	\$2,964,500,996	\$7,596,265,791	\$5,880,747,910	\$10,000,000	\$566,544,924	\$1,138,972,957	\$164,574,996
2004	2,800,502,661	8,572,712,312	6,479,560,217	10,000,000	714,703,053	1,368,449,042	175,821,371
2005	2,289,177,691	9,315,551,333	6,987,957,168	10,000,000	894,609,750	1,422,984,415	(26,874,316)
2006	2,187,127,996	9,731,935,336	7,027,814,464	10,000,000	902,979,820	1,791,141,052	298,745,535

The change over the examination period is as follows:

- 26.22% decrease in net written premium
- 28.07% increase in net admitted assets
- 17.37% increase in liabilities
- 57.96% increase in policyholder surplus
- 81.53% increase in net income

The Company reported net income of \$298.7 million for 2006, net loss of \$26.9 million for 2005 and net income of \$175.8 million for 2004. The net loss in 2005 was primarily the result of Hurricanes Katrina, Wilma, Rita and other natural disasters. The change in net income of \$325.6 million from 2005 to 2006 reflects significantly lower losses and loss expenses and other underwriting expenses incurred coupled with an increase in net investment gain. The reinsurance market was soft during 2005 and 2006 and there were abnormally high catastrophe losses in 2005.

ACCOUNTS AND RECORDS

The accounts and records reviewed included an evaluation of the Company's operational and organizational controls. The areas evaluated included computer systems, accounting systems, organizational structure and the processing structure. The Company operates in a computer-dominant environment, performs full system backups and rotates copies of programs and data files to its off-site storage facility on a weekly basis. The Company has a disaster recovery plan that covers its mainframe operations and that is periodically tested. It was determined that global controls surrounding the EDP environment were found to be sufficient.

FINANCIAL STATEMENTS

The following financial statements as determined by this examination are presented herein:

Analysis of Assets as of December 31, 2006 Liabilities, Surplus and Other Funds as of December 31, 2006 Underwriting and Investment Exhibit - Statement of Income, 2006 Capital and Surplus Account for the one year period ending December 31, 2006

It should be noted that the various schedules and exhibits may not add to the totals shown due to rounding.

Analysis of Assets **December 31, 2006**

	Ledger Assets	Nonadmitted Assets	Net Admitted Assets	Note
Bonds	\$5,623,296,899		\$5,623,296,899	(1)
Preferred stocks	10,487,500		10,487,500	
Common stocks	1,458,921,632		1,458,921,632	(2)
Cash and short-term investments	640,714,071		640,714,071	
Other invested assets	330,874,820		330,874,820	(3)
Receivables for securities	4,669,979		4,669,979	
Investment income due and accrued Agents' balances or premiums in course	81,014,070		81,014,070	
of collection Premiums, agents' balances and	336,214,323	\$ 888,243	335,326,080	
installments booked but deferred and not yet due	632,202,713		632,202,713	
not yet dde	032,202,713		032,202,713	
Accrued retrospective premiums	17,056,393	1,149,423	15,906,970	
Amounts recoverable from reinsurers Funds held by or deposited with	183,349,970		183,349,970	
reinsured companies	155,743,949	142,710	155,601,239	
Net deferred tax asset	342,323,326	168,008,746	174,314,580	
EDP equipment	254,475		254,475	
Furniture and equipment	3,657,031	3,657,031	0	
Receivables from parent, subsidiaries and Affiliates	15,780,901		15,780,901	
Aggregate write-ins for other than Invested assets	92,586,659	23,367,219	69,219,440	
Total assets	\$9,929,148,708	\$197,213,372	\$9,731,935,336	=

Liabilities, Surplus and Other Funds <u>December 31, 2006</u>

		Note
Losses	\$4,617,182,189	(4)
Reinsurance payable on paid losses and loss adjustment expenses	128,423,289	
Loss adjustment expenses	471,870,075	(4)
Commissions payable and contingent commissions	11,544,864	
Other expenses	45,321,529	
Taxes, licenses and fees	539,345	
Federal income tax payable	53,373,571	
Unearned premiums	969,581,751	
Ceded reinsurance premiums payable	385,305,304	
Funds held by company under reinsurance treaties	112,657,681	
Amounts withheld or retained by company for account of others	2,740,734	
Provision for reinsurance	4,703,066	
Net adjustments in assets and liabilities due to foreign exchange	24,997,001	
Payable to parent, subsidiaries and affiliates	14,567,800	
Aggregate write-ins for liabilities	185,006,265	(5)
Total liabilities	\$7,027,814,464	
Common capital stock	\$ 10,000,000	
Gross paid in and contributed surplus	902,979,820	
Unassigned funds (surplus)	1,791,141,052	
Chassigned funds (surplus)	1,791,141,032	
Surplus as regards policyholders	\$2,704,120,872	
Total liabilities and surplus as regards policyholders	\$9,731,935,336	

Underwriting and Investment Exhibit - Statement of Income Year Ended December 31, 2006

<u>Underwriting Income</u>	
Premiums earned	\$ <u>2,143,954,523</u>
Deductions:	
Losses incurred	\$1,330,831,437
Loss expense incurred	173,462,123
Other underwriting expenses	549,761,782
Total underwriting deductions	\$2,054,055,343
Net underwriting gain (loss)	\$ 89,899,180
Investment Income	
Net investment income earned	\$ 357,512,592
Net realized capital gains (losses)	33,234,491
Net investment income	\$ _390,747,083
Other Income	
Net gain (loss) from agents' or premium balances charged off	\$ 250,714
Aggregate write-ins for miscellaneous income (loss)	(13,001,257)
Total other income	\$ (12,750,543)
Net income before dividends to policyholders and federal income taxes	\$ 467,895,720
Federal and foreign income taxes incurred	169,150,184
Net income	<u>\$298,745,535</u>

Capital and Surplus Account December 31, 2006

Surplus as regards policyholders, December 31, 2005	\$ <u>2,327,594,165</u>
Net income	\$ 298,745,535
Change in net unrealized capital gains (losses)	126,856,653
Change in net unrealized foreign exchange capital gain	
(loss)	(3,127,164)
Change in net deferred income tax	57,017,445
Change in nonadmitted assets	(26,132,836)
Change in provision for reinsurance	(469,962)
Surplus adjustments: Paid in	8,370,070
Dividends to stockholders	(100,000,000)
Aggregate write-ins for gains and losses in surplus	15,266,967
Change in surplus as regards policyholders for the year	\$ <u>376,526,707</u>
Capital and surplus, December 31, 2006	\$ <u>2,704,120,872</u>

Schedule of Examination Adjustments

No adjustments were proposed for this examination.

NOTES TO FINANCIAL STATEMENTS

1) Bonds \$5,623,296,899

Investments in bonds are reported at values (amortized cost) adopted and approved by the Securities Valuation Office (SVO) of the NAIC. Bonds owned by the Company are as follows:

US Governments	\$	88,517,733
All Other Governments		227,322,810
States and Territories and Possessions		494,102,827
Political Subdivisions of States		670,256,999
Special Revenue	2	2,753,132,671
Public Utilities		101,085,486
Industrial and Miscellaneous	1	,288,878,373
Total	<u>\$5</u>	5,623,296,899

Bonds are designated by the SVO with the highest quality being "1" and lowest being "6". The Company held bonds rated as follows:

SVO Rating	<u>Amount</u>	Percent of Total
1	\$5,142,863,103	91.46%
2	320,750,586	5.71%
3	110,420,803	1.96%
4	44,549,907	0.79%
5	4,712,500	0.08%
Total	\$5,623,296,899	<u>100.00%</u>

Bonds with carrying values of \$1,187,098,589 were on deposit with various states or governmental (including foreign) insurance departments in compliance with insurance laws.

2) <u>Common Stock</u> \$1,458,921,632

Unaffiliated common stock is carried at market value. Affiliated common stock is carried at the underlying statutory equity basis.

<u>Type</u>	<u>Amount</u>
Investments in money market mutual funds	\$1,052,885,251
Unaffiliated publicly traded equity securities	152,691,561
Investments in affiliates	<u>253,344,820</u>
Total	<u>\$1,458,921,632</u>

3) Other Invested Assets

\$330,874,820

Other invested assets include limited partnerships and rabbi trusts. The limited partnerships are valued pursuant to the equity method of accounting which is prescribed by SSAP. The rabbi trusts are carried at market value. The Company has no individual investments in excess of 1% of admitted assets.

4) <u>Losses</u> Loss Adjustment Expenses

\$4,617,182,189 \$ 471,870,075

Losses and loss adjustment expenses (LAE) reserves represent 72.4% of the Company's liabilities as of December 31, 2006. Incurred but not reported (IBNR) reserves were 46.5% of loss reserves at year-end 2006.

INS Consultants, Inc. (INS) was retained by the Delaware Insurance Department to conduct a review of the Company's reserve methodologies and adequacy. INS evaluated the Company's book of business by line of business for loss and LAE. The conclusions reached by INS are largely based upon information supplied by the Company's staff, which included an indepth actuarial analysis. The INS reserve analysis was performed on both a gross and net of reinsurance basis and did not address the collectibility of reinsurance recoverables. The INS reserve review found the Company's combined net loss and LAE reserves were adequate to support the business underwritten.

The underlying data was tested through a review of open and paid claim files and actual payments made with no exceptions noted. The aggregated actuarial data provided by the Company was verified and reconciled to Schedule P of the Company's filed annual statement.

Loss and LAE reserves are subject to errors of estimation arising from the fact that the ultimate liability for claims evaluated as of the valuation date are dependent on future contingent events that cannot always be anticipated. The possible occurrence of such events, as well as the inherent uncertainty associated with statistical estimates, allows no guarantee that the actual ultimate liabilities will be the same as the reserve levels described in this examination report.

As a result of this study, INS has indicated a \$60,765,000 reserve change from the Company's reported amounts as follows:

<u>Item</u>	Reported By Company	INS Adjustment	Per Examination
Losses	\$4,617,182,189	\$59,066,000	\$4,676,248,189
Loss Adjustment Expenses	471,870,075	1,699,000	473,569,075
Totals	\$5,089,052,264	\$60,765,000	\$5,149,817,264

The financial change was not made due to materiality; please refer to subsequent events for more detail.

5) Aggregate Write-ins for Liabilities

\$185,006,265

The balance consists of the following components: \$98,736,628 due to affiliate under quota share agreement; \$81,670,488 reserve for uncollectible reinsurance; \$2,179,710 minimum pension liability; and \$2,419,439 in miscellaneous liabilities. Of the \$81,670,488 reserve for uncollectible reinsurance, \$61,961,000 relates to Founders Insurance Company (Founders), which is related to Centrix Financial, LLC (Centrix). Subsequent to the examination, the Company increased the reserve for uncollectible reinsurance an additional \$77,343,655 related to Founders. (See the Subsequent Events section of this report).

COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS

The summary of recommendations of the previous Report of Examination and the disposition of such items since that exam are as follows:

Previous Recommendation

Action by Company

1. It was noted that only one dividend payment, on March 25, 2002, was disclosed in the corresponding Form B of the annual Holding Company Registration Statement. Therefore, it is recommended that the Company disclose all dividends declared and paid in any given year on the appropriate Holding Company Registration Statement Form B where applicable.

The Company disclosed dividends declared in the corresponding Form B of the annual Holding Registration Statement for the years under examination, thereby complying with this recommendation.

- 2. It was observed during the review of inter-company transactions that the Company was settling expense charges with affiliated companies for which no service agreement existed. Furthermore, the existing inter-company service agreements previously described in the Agreements section of this report do not specifically allow for payments of convenience. This is a violation of 18 Del. C. §5005(a)(2)(d), which requires that all management agreements, service contracts and cost-sharing arrangements involving a domestic insurer and any person in its holding company system may not be entered into unless the insurer has notified the Commissioner in writing of its intention to enter into such transaction at least 30 days prior thereto. Therefore, it is recommended that the Company comply with 18 Del. C. §5005(a)(2)(d).
- 3. During the review of inter-company balances, it was observed that the Payable to Affiliates balance included \$69,490,855 due to affiliate ENIC for unapplied reinsurance proceeds not yet due under the 85% Global Quota Share reinsurance agreement. According to the NAIC Annual Statement Instructions Manual, amounts payable relating to inter-company reinsurance transactions are specifically excluded from Payable to Affiliates. As a result, this \$69,490,855 balance should be reclassified to Aggregate Write-ins for Liabilities from Payable to Affiliates. Therefore, it is recommended that the Company complete future annual statements in accordance with the NAIC Annual Statement Instructions Manual.

The Company had not resolved this issue as of December 31, 2006. However, effective January 1, 2008, the Company entered into a new service agreement among Everest affiliates, which lists all the entities and the load factor as well as addresses and allows for payments of convenience. Therefore, the Company has complied with this recommendation subsequent to the examination date but prior to the end of fieldwork.

The Company began properly classifying the balance due to affiliate ENIC related to reinsurance in the appropriate aggregate write-ins for liabilities line of the annual statement in 2005. The Company has complied with this recommendation.

RECOMMENDATIONS

No formal recommendations were made as a result of this examination.

CONCLUSION

The following schedule shows the results of this examination and the results of the prior examination with changes between examination periods.

<u>Description</u>	12/31/06 Current Examination	12/31/03 Prior <u>Examination</u>	Changes Increase (Decrease)
Assets	\$9,731,935,336	<u>\$7,599,139,855</u>	\$2,132,795,481
Liabilities	\$7,027,814,464	\$5,987,892,974	\$1,039,921,490
Common capital stock Gross paid in and contributed surplus Unassigned funds (surplus) Total capital and surplus	\$10,000,000 902,979,820 <u>1,791,141,052</u> \$2,704,120,872	\$10,000,000 566,544,924 1,034,701,957 \$1,611,246,881	\$0 336,434,896 <u>756,439,095</u> \$1,092,873,991
Totals	\$9,731,935,336	<u>\$7,599,139,855</u>	\$2,132,795,481

In addition to the undersigned, acknowledgment is made of the assistance provided by the Delaware Insurance Department's consulting actuarial firm, INS Consultants, Inc.

Respectfully submitted,

Joseph J. Murano, CFE

Joseph M mars J.

Examiner-in-Charge

State of Delaware

Northeastern Zone, NAIC

SUBSEQUENT EVENTS

1.) <u>Service Agreement</u>

Effective January 1, 2008, the Company entered into a service agreement with all affiliates of the Everest Re Group, thereby replacing the existing individual service agreements with affiliates previously mentioned under the "Agreements" section of this report. Each affiliate agrees to provide administrative, consultative and other support services to the other affiliates as needed. In return, the recipient affiliate agrees to pay the service-providing affiliate 108% of its costs and expenses incurred in providing those services. The new service agreement, which was approved by the Delaware Department of Insurance on January 31, 2008, addresses and allows for payments of convenience.

2.) The Company sold its United Kingdom (U.K.) Branch on January 1, 2004, to Everest Re Reinsurance Bermuda Ltd., a subsidiary of the Company's ultimate parent, Everest Re Group, Ltd. The sales agreement included a fixed sales price of \$77 million in exchange for the net assets of the U.K. Branch. The Company realized a net capital loss of \$3,950,800 on the sale. In connection with the sale, the Company provided a reserve indemnity agreement providing for indemnity payments of up to 90% of \$44.51 million of the excess of 2002 and prior loss and LAE reserves, provided that any recognition of profit from the reserves for 2002 and prior underwriting years are taken into account. The Company is fully reserved under this reserve indemnity agreement as of December 31, 2006. Currently, the Internal Revenue Service is reviewing the calculation of the net realized capital gain or loss on the sale transaction and a final determination has not yet been made.

- 3.) Subsequent to the examination date, the Company was in litigation with Founders Insurance Company related to the excess of loss reinsurance agreement covering the Centrix program. As of December 31, 2007, the net impact to the Company is approximately \$156,851,000, which is in excess of 5% of surplus. The Company has established a reserve for uncollectible reinsurance.
- 4.) Subsequent to the examination date the Company entered into arbitration with London Life Reinsurance Group related to the aggregate stop loss reinsurance contracts in effect for accident years 1999, 2000 and 2001. On March 1, 2008 the Company received notification that an arbitration panel ruled against the Company on the 2001 accident year only. The Company returned collateral drawn down and rescinded the 2001 contract. The effect of this ruling on the Company's surplus is a decrease of \$45,598,421.
- 5.) The Company formed and funded a wholly owned subsidiary, Mt. Whitney Securities, Inc. (Delaware) on June 1, 2007, via a transfer of the Company's equity portfolio. The market value of the securities at the time of the transfer was \$850.6 million. This transaction was approved by the Delaware Insurance Department.
- 6.) During the fourth quarter of 2007, the Company booked significant increases in asbestos loss reserves. The Company booked additional reserves of \$250 million with respect to reinsurance operations. The reserve increase reflects unfavorable loss development in the 1997 and prior accident years.
- 7.) The Company issued modified property insurance coverage, in connection with a program administered by Centrix Financial, LLC (Centrix), commencing in August 2003. That program was in run-off by the second quarter of 2006. Under the program, Centrix originated substandard vehicle loans primarily through credit unions. The insurance

provides coverage if a series of events occur. First, the borrowers must make the first payment on the loan; second, the underlying loan must default; third, the vehicle must be repossessed and then finally the vehicle must be sold at auction. If any of those four conditions are not met, the Company is not liable. If all of the events occur, and other terms and conditions in the policy are satisfied, the Company will reimburse the insured for the difference between the outstanding loan balance and the deemed proceeds from the sale of the car in accordance with the terms of the policy.

The Company cedes 100% of losses exceeding a 20% per loan year claim frequency rate to Everest Re, who in turn, cedes 100% of the amount to Founders Insurance Company ("Founders"), an affiliate of Centrix. The Company further cedes 85% of the losses retained by it to Everest Re under an inter-company Reinsurance Agreement. Currently the Company and its affiliates are involved in litigation with Centrix, Founders, and several principals and/or former officers of those entities.